## APPENDIX

Revenue Act of 1942, c. 619, 56 Stat. 798:

> SEC. 121. NON-TRADE OR NON-BUSINESS DEDUCTIONS.
>
> (a) *Deduction for Expenses.*—Section 23 (a) (relating to deduction for expenses) is amended to read as follows:
>
> "(a) *Expenses.*—
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> * * * * *
>
> "(2) *Non-Trade or Non-Business Expenses.*—In the case of an individual, all the ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income."
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> * * * * *
>
> (e) *Retroactive Amendment to Prior Revenue Acts.*—For the purposes of the Revenue Act of 1938 or any prior revenue Act the amendments made to the Internal Revenue Code by this section shall be effective as if they were a part of such revenue Act on the date of its enactment. (26 U. S. C., Supp. IV, Sec. 23.)

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

> ART. 23 (a)–15 [as added by T. D. 5196, 1942–2 Cum. Bull. 96, 97–100 [1]]. *Nontrade*

[1] This article was also amended by T. D. 5280, 1943 Cum. Bull. 1022, and T. D. 5331, 1944 Cum. Bull. 98, but such amendments are in no respect material here.

*or Nonbusiness Expenses.*—(a) *In general.*—Subject to the qualifications and limitations in Chapter 1 and particularly in section 24, as amended, an expense may be deducted under section 23 (a) (2) only upon the condition that:

(1) it has been paid or incurred by the taxpayer during the taxable year (i) for the production or collection of income which, if and when realized, will be required to be included in income for Federal income tax purposes, or (ii) for the management, conservation, or maintenance of property held for the production of such income; and

(2) it is an ordinary and necessary expense for either or both of the purposes stated in (1) above.

The term "income" for the purpose of section 23 (a) (2) comprehends not merely income of the taxable year but also income which the taxpayer has realized in a prior taxable year or may realize in subsequent taxable years; and is not confined to recurring income but applies as well to gains from the disposition of property. For example, if defaulted bonds, the interest from which if received would be includible in income, are purchased with the expectation of realizing capital gain on their resale, even though no current yield thereon is anticipated, ordinary and necessary expenses thereafter incurred in connection therewith are deductible. * * *

Expenses, to be deductible under section 23 (a) (2), must be "ordinary and necessary," which presupposes that they must be reasonable in amount and must bear a reasonable and proximate relation to the

production or collection of taxable income or to the management, conservation, or maintenance of property held for the production of income.

(b) Except for the requirement of being incurred in connection with a trade or business, a deduction under this section is subject to all the restrictions and limitations that apply in the case of the deduction under section 23 (a) (1) (A) of an expense paid or incurred in carrying on any trade or business. * * *

Capital expenditures, and expenses of carrying on transactions which do not constitute a trade or business of the taxpayer and are not carried on for the production or collection of income or for the management, conservation, or maintenance of property held for the production of income, but which are carried on primarily as a sport, hobby, or recreation are not allowable as nontrade or nonbusiness expenses.

* * * * *

Expenditures incurred in defending or perfecting title to property, in recovering property (other than investment property and amounts of income which, if and when recovered, must be included in income), or in developing or improving property, constitute a part of the cost of the property and are not deductible expenses. Attorneys' fees paid in a suit to quiet title to lands are not deductible; but if the suit is also to collect accrued rents thereon, that portion of such fees is deductible which is properly allocable to the services rendered in collecting such rents. Expenditures incurred in protecting or asserting one's rights to property of a decedent as heir or

legatee, or as beneficiary under a testamentary trust, are not deductible expenses. Expenditures incurred for the purpose of preparing tax returns (except to the extent such returns relate to taxes on property held for the production of income), for the purpose of recovering taxes (other than recoveries required to be included in income), or for the purpose of resisting a proposed additional assessment of taxes (other than taxes on property held for the production of income) are not deductible expenses under this section, except that part thereof which the taxpayer clearly shows to be properly allocable to the recovery of interest required to be included in income.

* * * * *

PAR. 10. Pursuant to the above provision of law, the amendments to sections 19.23 (a)–15, 19.23 (l)–1, 2, and 3, and 19.24–4 of Regulations 103 set forth in this Treasury decision (which regulations cover taxable years beginning after December 31, 1938), are hereby made applicable to taxable years beginning prior to January 1, 1939 (such years being covered by Regulations 101, 94, 86, 77, 74, 69, 65, 62, 45, and 33).

* * * * *

ART. 24–2. *Capital expenditures.*— * * * The cost of defending or perfecting title to property constitutes a part of the cost of the property and is not a deductible expense. The amount expended for architects' services is part of the cost of the building. Commissions paid in purchasing securities are a part of the cost price of such securities. Commissions paid in selling securities, when such commissions are not an

ordinary and necessary business expense,[2] are an offset against the selling price. Expenses of the administration of an estate, such as court costs, attorneys' fees, and executors' commissions, are chargeable against the corpus of the estate and are not allowable deductions. Amounts to be assessed and paid under an agreement between bondholders or shareholders of a corporation, to be used in a reorganization of the corporation, are investments of capital and not deductible for any purpose in returns of income. * * *

H. Rep. No. 2333, 77th Cong., 2d Sess., pp. 46, 74–75 (1942–2 Cum. Bull. 372, 410, 429–430):

6. NONTRADE OR NONBUSINESS DEDUCTIONS

The existing law allows taxpayers to deduct expenses incurred in connection with a trade or business. Due partly to the inadequacy of the statute and partly to court decisions, nontrade or nonbusiness expenses are not deductible, although nontrade or nonbusiness income is fully subject to tax. The bill corrects this inequity by allowing all of the ordinary and necessary expenses paid or incurred for the production or collection of income or for the management, conservation, or maintenance of property held for the production of income. Thus, whether or not the expense is in connection with the taxpayer's trade or business, if it is expended in the pursuit of income or in connection with property held for the production of income, it is allowable.

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[2] See explanation of this clause given in G. C. M. 15430, below, which was approved by this Court in *Spreckels* v. *Helvering*, 315 U. S. 626.

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For an expense to be deductible under this section, it must have been incurred either (1) for the production or collection of income, or (2) for the management, conservation, or maintenance of property held for the production of income. Ordinary and necessary expenses so paid or incurred are deductible under section 23 (a) (2) even though they are not paid or incurred for the production or collection of income of the taxable year or for the management, conservation, or maintenance of property held for the production of such income. The term "income" for this purpose comprehends not merely income of the taxable year but also income which the taxpayer has realized in a prior taxable year or may realize in subsequent taxable years, and is not confined to recurring income but applies as well to gain from the disposition of property. Expenses incurred in managing or conserving property held for investment may be deductible under this provision even though there is no likelihood that the property will be sold at a profit or will otherwise be productive of income.

* * * * *

A deduction under this section is subject, except for the requirement of being incurred in connection with a trade or business, to all the restrictions and limitations that apply in the case of the deduction under section 23 (a) (1) (A) of an expense paid or incurred in carrying on any trade or business.

* * * * *

S. Rep. No. 1631, 77th Cong., 2d Sess., pp. 87–88 (1942–2 Cum. Bull. 504, 570–571), contains an explanation of the statutory provisions involved in the instant case which is almost identical with H. Rep. No. 2333, *supra*.

G. C. M. 15430, XIV–2 Cum. Bull. 59–61 (1935):

> An opinion is requested whether commissions paid in connection with sales of securities are deductible as ordinary and necessary business expenses under section 23 (a) of the Revenue Act of 1934, or whether they should be used as an offset against the selling price of the securities in computing gain or loss.
>
> The question as to the deductibility of such commissions involves three classes of taxpayers—(1) a dealer in securities, (2) a trader in securities, and (3) a taxpayer who purchases and sells securities occasionally but not in such quantities or under such circumstances as to constitute him either a dealer or a trader. * * *
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> * * * The position of the Treasury Department, which has been in effect for many years, is expressed by paragraph 108 of Regulations 33, revised, construing the Revenue Act of 1916, which provides that:
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> "*Expense—Commissions paid.*—Commissions paid in purchasing and selling securities are a part of the cost or selling price of the securities and not otherwise deductible. They do not constitute expense deductions in a return of income."
>
> Article 293 of Regulations 45 reads in part as follows:
>
> "* * * Commissions paid in purchasing securities are a part of the cost price of such securities. Commissions paid in sell-

ing securities are an offset against the selling price. * * *"

The same language appears in article 293 of Regulations 62, article 292 of Regulations 65, article 292 of Regulations 69, and article 282 of Regulations 74. Article 282 of Regulations 77 and article 24–2 of Regulations 86 read in part as follows:

"* * * Commissions paid in purchasing securities are a part of the cost price of such securities. Commissions paid in selling securities, *when such commissions are not an ordinary and necessary business expense,* are an offset against the selling price. * * *" [Italics supplied.]

The language of all the Revenue Acts from the Revenue Act of 1913 to and including the Revenue Act of 1934 is substantially identical in so far as the provisions affecting the present issue are concerned. It is well settled that where a statute has been construed for a long period of time as having a certain meaning, a reenactment of that statute without change indicates legislative sanction of the construction previously given it.

* * * * *

Since, fundamentally, commissions on both purchases and sales are direct charges to the profit or loss arising from the particular sales in connection with which they are paid, there can be no justification for a departure from that method of treatment except in those cases where the detail of accounting on that basis is so burdensome as to make its use impracticable. No such accounting difficulties exist in the case of any of the three classes of taxpayers enumerated above except the *dealer.* Both the occasional seller and the trader are re-

quired to account in their income tax returns for the profit or loss on each individual sale. The right to inventory securities is denied to the trader and to the occasional seller. (See article 22 (c)–5, Regulations 86.) In so accounting, no difficulty whatever is experienced in adding the purchase commission to the cost of the security and deducting the sale commission from the selling price thereof. In the case of the dealer, no accounting difficulty is experienced in adding the purchase commission to the cost and he is required to do so in all cases instead of treating such commissions as current expenses even where he is permitted to inventory his securities. However, in the dealer's accounting there are difficulties which make it impracticable for him to match his selling commissions against each individual sale. The dealer usually buys in large quantities, his sales are numerous and in relatively small amounts, his commissions are often computed and paid on a volume of sales instead of on individual transactions, and where he uses inventories he necessarily departs widely from the principle of accounting for the profit on each individual purchase and sale. The Commissioner has recognized these difficulties and in actual practice has permitted the dealer in securities to treat his selling commissions as "ordinary and necessary business expenses," not because they are technically such but because of practical considerations. However, no formal recognition was given this practice until the promulgation of Regulations 77, when, in article 282, there was inserted the qualifying phrase "when such commissions are not an ordinary and necessary business expense." This language should not be

construed as holding that selling commissions are to a trader "ordinary and necessary expenses * * * in carrying on any trade or business" within the meaning of section 23 (a) of the Revenue Act of 1934 and corresponding provisions of prior Revenue Acts.

* * * * *

It is concluded, therefore, that buying commissions are a part of the cost of securities and are not deductible as ordinary and necessary business expenses. Selling commissions are an offset against the sale price and are not deductible as ordinary and necessary business expenses, except in the case of a dealer in securities.

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